

**Inv. No. TA-204-09: Certain Steel Products
(Stainless Products)**

Testimony of

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Thank you, Chairman Okun and Commissioners, for this opportunity to appear in this proceeding to examine the progress made by the US producers of stainless steel products under the Section 201 relief program. I am Charles Blum of International Advisory Services Group, appearing on behalf of the European Confederation of Iron and Steel Industries (EUROFER). With me is Christopher Ryan of the law firm of Shearman & Sterling, appearing on behalf of Arcelor, the largest member company of EUROFER.

EUROFER has a strong interest in this proceeding for several reasons. First, our members are leaders in the global stainless steel industry. According to the International Stainless Steel Forum, the Arcelor Group, ThyssenKrupp Stahl, the Acerinox Group and AvestaPolarit are the four largest stainless steel producers in the world. In addition, we have a number of smaller producers which occupy important niches in stainless and other specialty steel production. Second, imports from covered countries, and from Europe in particular, have been reduced by this relief, even though historically we have been responsible trading partners with the United States. Third, Europeans have been for some time the leading foreign investors in the American stainless industry, and we are continuing to invest here. We want this sector to return to profitability so that we can make money here, too.

To begin, I will examine the steps made by the domestic industry toward a positive adjustment. Mr. Ryan will then address several issues arising out of the domestic industry's pre-hearing brief.

What's At Issue in This Proceeding?

As we argued in our general brief filed on behalf of EUROFER, a central issue for this mid-term review is the adequacy of the adjustment effort made by each industry and whether continuation of Section 201 relief will facilitate further adjustment to import competition. The President's aim in taking this action was to give each of the 14 steel industries a chance to make changes that would improve their competitiveness for the long-run. There was no guarantee of success, but only of the chance to make needed changes and to do so without delay. So, the major questions are: have the US producers taken steps to improve their long-run competitiveness, and will continuation of such relief remedy existing problems that may hinder the industry's ability to compete? The answer to the first question is, yes; as the data show the industry has taken a number of effective steps to enhance its competitiveness. The answer to the second question is, no; further relief will only serve to sustain marginal producers to the detriment of the stronger firms within the industry.

In our brief, we made several points that bear repeating here:

- Adjustment is a broad concept that encompasses all efforts to restructure, reduce costs, and increase revenues. No one size fits all. Rather, each company must elaborate its own route to competitiveness, if it is willing and able to do so.

- The Commission and the President should recognize that adjustment often entails *up-front costs* that promote competitiveness over the *long-run*. You have to spend money to make money. Consolidations, new investments, workforce reductions and other steps must be paid for immediately, but they can produce a stream of benefits for the future.
- Finally, the Commission and the President should consider the adjustment process as inherently competitive. Not all companies, and certainly not all facilities, can be winners. Thus, the USITC and the President should make its judgment based on the *industry as a whole*, not the weakest individual member.

Each of these points will be illustrated by developments in the stainless steel industry since March 2002.

The Adjustment Track Record

Section 201 is extraordinary relief with an extraordinary purpose – to permit a domestic industry to adjust to import competition. How the adjustment is to be made is a matter for companies to decide individually and in competition with one another. Not all firms will necessarily succeed.

It is striking that a majority of the 21 reporting firms in the three stainless industries failed to submit an adjustment plan to the Commission or the Executive

Branch. (PSR, Table STAINLESS IV-1) To be perfectly fair, only eight of the 21 responding companies actually acknowledged that they had failed to do so. Three others could not recall for certain whether they had or not! For most of the domestic firms, the adjustment aspect of the 201 process seems to have been just a minor detail or perhaps a major annoyance. What does this say about the seriousness of purpose of these industries in making themselves fit competitors for the long-run?

We would also call the Commission's attention to the rather curious language of the domestic industry's description of the adjustment process. Referring to stainless wire, their pre-hearing brief laments that the US producers have been "*forced* to reduce costs." (CSS brief at 9, emphasis added) They speak of cost-cutting as a bitter medicine or some form of punishment rather than as a necessary ingredient to long-run competitiveness! This language also betrays a curious lack of urgency on the part of some US producers, particularly in view of their claims of long-term damage from imports. We fail to understand why this central aspect of the 201 process seems of such little importance to some stainless producers.

Despite the lack of enthusiasm for adjustment measures from some US producers, the industry as a whole has made substantial progress over the 15 months relief has been in place, generally in terms of raising productivity and lowering costs. As a result, today the industry overall is better able to compete with imports. You will find examples from a substantial majority of the reporting firms in the confidential Appendix F to the Pre-Hearing Staff Report.

One of the most notable successes was that of a wire producer that was able to effect a dramatic turnabout in its bottom line by making one modest investment and several operational changes. (BPI material cited in the CSS brief at 13 and 29 and PSR at p. F-41) This success demonstrates the principles that a positive adjustment does not necessarily require huge amounts of capital and that *timely* changes can produce dramatic positive results even before home market demand has recovered. This company didn't wait for better times; it acted, and now it's profitable.

The Cartech experience is also instructive. As one of the largest producers of all three products under examination in this hearing, Cartech's financial performance heavily influences the industry's overall numbers. In its most recent quarterly report dated May 14, Cartech provided multiple indications of a company on the rebound:

- Net income was \$1.7 million, compared to a loss of \$10.5 million in the same period in 2002.
- Gross margins were up 410 basis points to 15.3 percent versus 11.2 percent a year earlier.
- The improvement was attributed to "cost reduction efforts that resulted in a lower cost structure and productivity improvements."
- Selling and administrative expenses were reduced by 14 percent (\$6.9 million). More than half the improvement was due to reduced employment costs. Overall, the company eliminated 500 jobs.

- Interest expense was reduced by about seven percent due to lower debt levels and lower interest rates on floating rate debt.
- Even the results for second half of the 2002 need to be interpreted in light of \$27 million in special accounting charges for reductions in the workforce (\$17.4 million), pension plan curtailment loss (\$6.7 million) and the write-down of certain assets (\$2.9 million). Of this amount, \$14.2 million was incurred in Cartech's first quarter (July-September) and \$12.8 million in the second (October-December).

Cartech's experience serves as an excellent illustration of our point that structural changes often entail up-front costs that, once made, can provide a stream of benefits into the future. The crucial need is to act in a timely and decisive way.

Overall, the reporting firms have made a number of significant changes with rather modest amounts of money. In that regard, the Commission may find the trend in the industries' capital expenditures to be of particular interest. (See the BPI data contained in Tables STAINLESS C-1, 2 and 3 of the Pre-Hearing Staff report.) The consistent trend in these numbers over the three-year period and from one product to the next is striking.

Finally, it's truly impressive that the domestic industry witnesses managed to submit a pre-hearing brief that studiously avoids the single biggest change in the stainless bar and rod industries – the imminent entry of North American Stainless as a domestic

producer. NAS, a subsidiary of Acerinox, is completing a state of the art 100,000 metric tons per year bar and rod facility at Ghent, Kentucky, where it already produces 800,000 of raw stainless steel. To gauge the size of this new capacity relative to existing capacity, the Commissioners might find it interesting to consult the BPI data on Tables STAINLESS III-1 and III-2 of the Pre-Hearing Staff Report.

NAS's entry will change the competitive facts of life in the US stainless bar and rod industries. The size and expected quality of the new mill in Kentucky will be enough to make the US industry as a whole far more competitive with imports. Indeed, the major challenge for the firms now in those businesses will be to compete with *domestic* competition, not imports.

The stated strategy of waiting to make needed improvements until financial performance has improved (CSS brief at 21: "As the economy improves, the domestic industry's financial situation should increase to profit levels where it can make the investments required to be able to compete with imports.") seems odd for several reasons. First, the best time to raise funds would be while relief is at its maximum level. With tariffs falling each year and the possibility that the President might reduce or even terminate the relief, why wait? Second, domestic competitors are not standing still. They're moving on their own plans and getting results. Third, the US industry is aware of the promising forecasts of stainless demand. The ISSF expects an all-time record year in 2004 worldwide, with strong growth in Asia and Central and Eastern Europe combined with recovery in North America and Western Europe. If record demand is expected as

early as next year, why not act now to lower costs, improve quality and adjust the product mix to the market? Why wait until the order book is fuller and physical changes to facilities will hinder the mills' capability to make and deliver steel?

Why Relief Should Be Terminated

In conclusion, let me cite three reasons why relief on these three stainless steel products should be terminated:

First, global demand is rising and is expected to reach record levels next year. This will open new opportunities for competitive US producers, even if domestic demand recovers at a slower rate. They are being presented with a golden opportunity to establish themselves as worthy competitors in a growing global market.

Second, the domestic industry has recovered substantial domestic market share and been given a new chance to solidify relations with customers. Most of the domestic firms have already taken steps to improve the costs or quality of their product and reposition themselves in the market. There is a considerable amount of new, state-of-the-art capacity coming on stream to serve the domestic and world markets.

Third, in adjustment terms, most members of the industry have set modest objectives and achieved them. Whether those steps are adequate will be judged by

competition -- both domestic and international -- in the marketplace. The US stainless industry has had a fair opportunity to make the changes it deemed necessary. Further relief will only serve to sustain marginal producers to the detriment of the stronger firms within the industry. There is scant justification for continuing relief.